USDA Foreign Agricultural Service

GAIN Report

Global Agriculture Information Network

Template Version 2.09

Voluntary Report - public distribution

Date: 4/21/2004

GAIN Report Number: CH4807

China, Peoples Republic of

Market Development Reports

High Value Ag Products: What Is China Really Importing?

2004

Approved by:
Ross Kreamer
U.S. Consulate

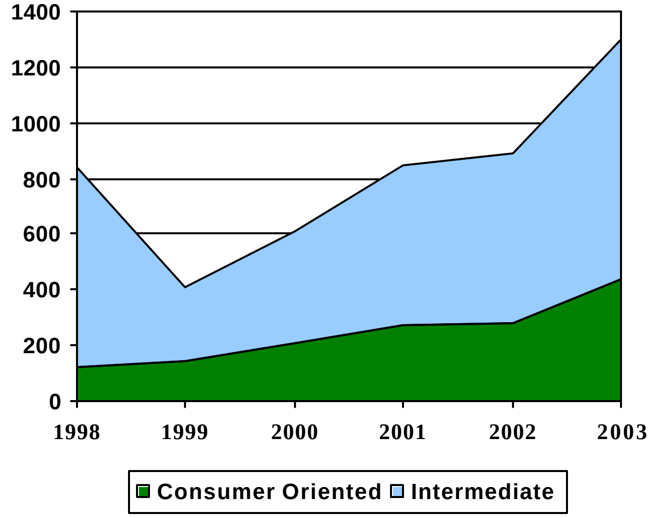
Prepared by:
Ralph Bean

Report Highlights:
On-the-ground evidence in Shanghai indicates that China is importing a growing variety of high value added products from the U.S., primarily for use in manufacturing. Close examination of the trade statistics confirms this, and reveals several important trends in China's imports from the U.S. China's high-value imports are undergoing a transformation mirroring that of the economy as a whole.

Includes PSD Changes: No
Includes Trade Matrix: No
Unscheduled Report
Shanghai ATO [CH2]
[CH]

What Lies Beneath

U.S. Exports to China, by Category
1998 – 2003 ($ Million)



Source: U.S. Customs Data

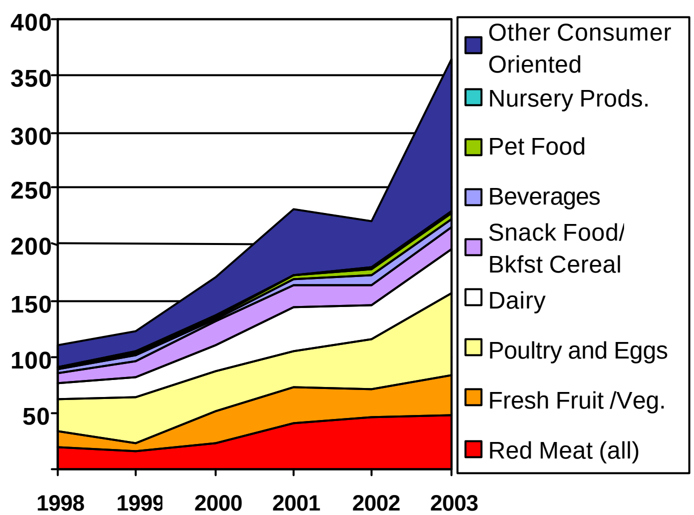
China's imports of processed food and intermediate agricultural products have grown quickly over the past five years. At the same time, however, the content of these imports has shifted sharply, with highly specialized and high value products gaining ground at a blistering pace. This movement into specialized imports has led to an increase in the number of types of products being imported and placed existing classification schemes under pressure. Broad classifications, though useful, often conceal as much as they reveal. To see what China is really importing from the U.S., and what it means for future exports, it has become more important than ever to delve beneath the surface of the trade statistics and see what lies beneath.

A Banner Year

2003 was a banner year for U.S. exports of high-value agricultural goods to China. Exports of intermediate products jumped by almost 42% to reach $863 million, while consumer-oriented goods increased by over 55% for a total of $439 million in 2003. Over the past six years, U.S. exports of consumer-oriented products to China have increased at average rate of 30% per year. At the same time, the mix of commodities being exported has changed, in many cases moving into more highly-specialized items. Most of these products fall into one of three types: commodities for processing, ingredients for food production and high-value consumer goods. All reflect the increasing sophistication of China's processing industries and consumers.

<u>Consumer-Oriented Goods</u>

U.S. Exports of Consumer-Oriented
Food Products to China, 1998-2003 ($million)

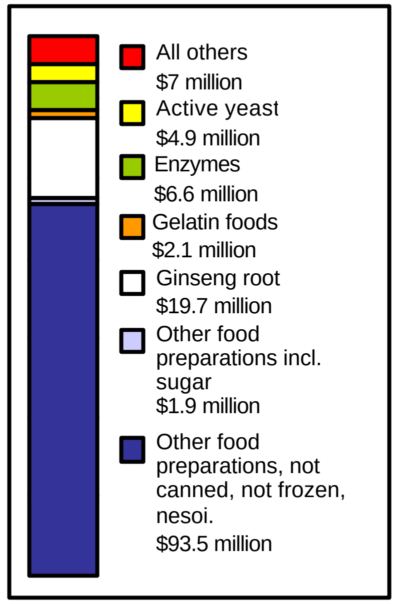


Source: U.S. Customs Data

China's imports of consumer-oriented products from the U.S. have grown rapidly, nearly quadrupling in size over the past six years. Although this category includes poultry, processed fruits and vegetables, and beef, it is now dominated by 'other consumer oriented.' This grab-bag category has been a significant component in China's imports from the U.S. for a number of years, but in 2003, imports of 'other' more than doubled, reaching $136 million and accounting for more trade than poultry and beef combined. The sheer size of this category, not to mention its explosive growth, makes close examination imperative. A number of other other categories of consumer goods also merit close examination for the trends they conceal.

Other – The $93 million mystery. Of the $136 million in trade accounted for by this category, over $93 million (68%) falls under a single tariff line: the poetically named “other food preparations, not elsewhere specified, not canned, not frozen, not including sugar,” HTS code 2106907090. The next largest component item, ginseng root (wild and cultivated combined), remains a distant second at less than $20 million. (Industry sources claim that as much as half of U.S. cultivated ginseng exports actually originate in Canada). Efforts to track down the exact content of ‘other’ have yielded only the sparsest insights. The category may include mixtures of different fruits and vegetables, provided they are ‘transformed’ into a sauce or soup—and are not canned or frozen or contain sugar. Bulk or bottled products may fit into this category, but not jellies or jams (which contain added sugar). Similar mixtures including mixed meat or dairy products are also possibilities. One source notes that certain types of fortified concentrated orange juice may be part of this, since the addition of extra calcium, etc., may cause the product to fall outside the normal classification for orange juice concentrate. Attempts to track the content using Chinese Customs data yielded similar results. Despite ATO’s best efforts, the exact composition of this $93 million in trade remains a frustrating mystery.

U.S. Exports of ‘Other’ Consumer-Oriented Foods By Category, 2003



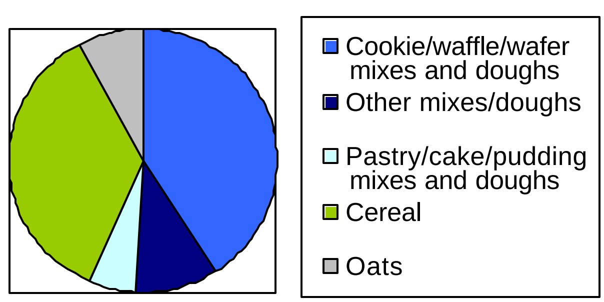
Source: U.S. Customs Data

Processed Fruits and Vegetables – Frozen potatoes are the primary component in this category, accounting for nearly half of sales and with a growth rate of 12% in 2003. Raisins and frozen sweet corn showed the fastest growth among major products at 98% and 89%, respectively, with sales at $5.9 and $6.6 million. The biggest surprise in 2003 was a massive surge in imports of strawberry products. Frozen strawberry imports jumped from a mere $18,000 in 2002 to nearly $3 million in 2003. Likewise, prepared and preserved strawberry exports jumped from $0 in 2002 to $923,000 in 2003. Anecdotal evidence indicates that frozen strawberries are being imported for processing into dried strawberry chips, then re-exported. Prepared and preserved peaches imports also jumped, going from $0 to nearly $1.6 million in 2003.

Fresh Fruit – Although oranges continue to dominate, the biggest surprise was, once again, strawberries. U.S. Customs data show a massive surge in fresh strawberry imports from $350,000 to over $5 million. There is no import protocol for fresh strawberries to China, however, and China Customs does not show a corresponding rise, so this is most likely the result of an error in the data. Examination of trade data for Hong Kong and Taiwan indicate that the shipment to these destinations were not accidentally attributed to mainland China. Where the confusion lies, in the product or the destination, remains unknown.

Breakfast Cereals – Although small, this category is notable for a hidden trend. The bulk is not composed of breakfast cereal at all, but of baking mixes and dough, which at over $1 million, account for more than half of the total. Other types of frozen pastry products and breads appear are scattered across

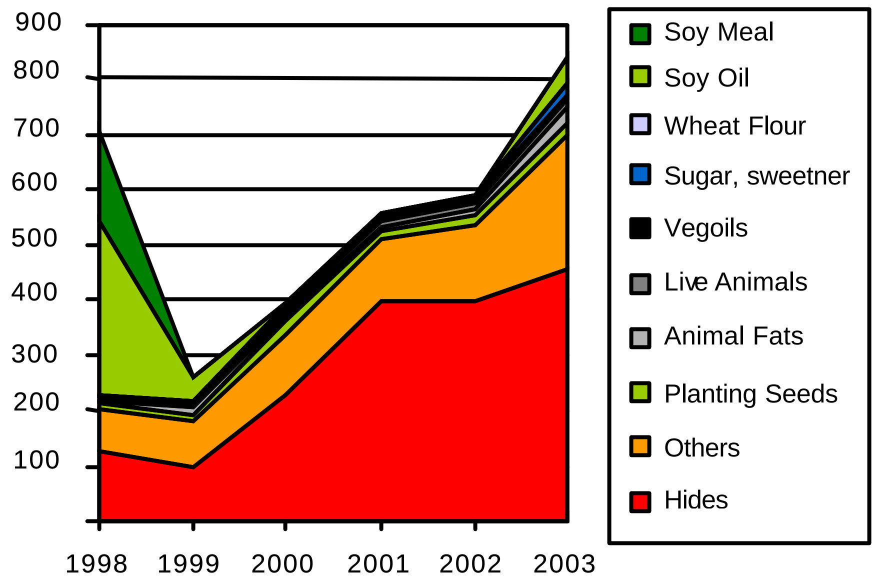
Breakfast Cereal: 1993 U.S. Exports To China, By Product Description



different categories, helping to conceal the fact that all have seen substantial increases in exports. Although still a relatively small item, it is clear that pastry products are becoming an increasingly popular export item for the China markets. Anecdotal evidence implies that demand is being driven by the growing number of coffee shops that stock western-style pastries and the bakeries that supply them. (Exports of coffee-related items such as creamers are also growing). Dough and mix imports are likely to continue growing: Mrs. Field's has set up shop in the Shanghai area, and is reportedly importing frozen dough directly from the U.S.

Intermediate Products

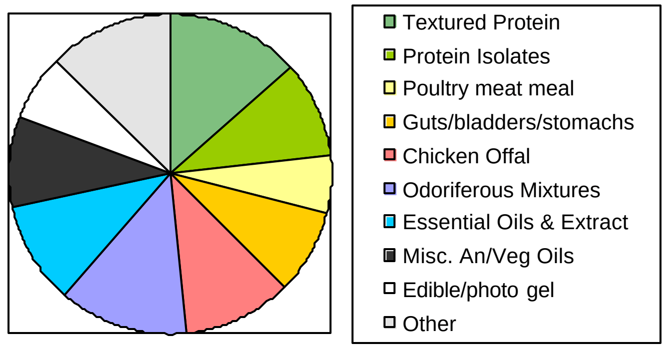
U.S. Exports of Intermediate Products to China
1998 – 2003 ($Million)



Exports of intermediate products to China collapsed in 1999, but have gradually recovered over recent years and now exceed 1998 levels. Prior to 1999, exports were dominated by soybean oil and meal. The collapse in soy products imports was a partly a result of the development of China's domestic soy processing industry, which led to a switch in imports from processed products to whole soybeans for processing. China's soybean imports from all destinations skyrocketed beginning in 1999. The recovery in intermediate products exports since then has been led by hides and skins . . . and by 'other' intermediate commodities. As a result, the specific content of intermediate commodities exports has undergone a complete transformation, with bovine hides now the largest single product, followed by 'other.' The vast majority of the hides are destined for China's burgeoning manufacturers of footwear, clothing and furniture. Although large quantities of the finished products remain in China, the bulk are exported. 'Other intermediate' is now the second largest category behind hides, accounting for nearly a quarter of a billion dollars in U.S. exports in 2003. In fact, excluding hides and skins, 'other' now accounts for more trade than all other intermediate products combined. What little is left after subtracting these two, consists largely of planting seeds, animal fats and sweetners.

Thankfully, unlike consumer-oriented products, the 'other products' category for intermediate products yields more readily to analysis. No single type of product dominates, although processed proteins constitute two of the top five. Essences and aromatic substances for use in food and non-food products are also prominent, along with chicken offal (mostly feet) and guts, bladders and stomachs from livestock. Many, such as the protein products and essences, are specialized products for use in food processing or manufacturing. The essences and vegetable saps, for example, break down further into dozens of specific tariff lines including mint oils, hops extracts and other items. To give an idea of how important these specialized products are becoming to U.S. exports, consider that that in 2003 exports to the U.S. of a single tariff line, 'concentrated and textured protein substances' from the U.S. amounted to nearly as much as its imports of U.S. wheat. (Many of these products are also used in non-food applications: aromatic substances are used in aromatic candles, soaps and shampoos, while some of the essences can be used in products such as toothpaste. Another point to note is the dominance of proteins, not just in the form of processed ingredients, but in poultry offal, poultry meal and livestock offal. Taken in combination with China's imports of U.S. meat and poultry in the consumer-oriented category and massive imports of soybeans, China's demand for protein of all types takes on new dimensions.

U.S. Exports of 'Other' Intermediate products to China by Category, 2003



The Importance of Being 'Other'

It is no coincidence that 'other' products have become so prominent in U.S. food exports to China, nor that these categories are among the fastest growing. For both intermediate goods and consumer-oriented products, this growth reflects the increasing complexity and uneven growth of China's economy. Many of the products in demand are so specialized as to defy easy classification, creating a sudden jump in imports of 'other' products.

Consumer-oriented imports are increasingly leaning in two directions. The first consists of traditional high-value items in short supply, such as offal, high quality meat and poultry products and nuts. The second consists of 'niche' products for which demand exists, but is not concentrated enough to support the development of a domestic industry. This includes 'foreign' taste foods and specialty products (infant formula, fortified foods, etc.). Premium and exotic products, for which consistent but scattered demand exists, also fit into this category. Demand may shift between specific products, but overall likely to continue growing. Anecdotal evidence seems to indicate that this is where most of the $93 million in 'other food preparations' falls, but until more information becomes available there is no way to be certain. The consumer-oriented products category also, however, includes a number of products like whey, that are used as ingredients, and subject to different market forces.

Ingredients for use in manufacturing are also driving growth in 'other' intermediate products, the bulk of which consists of protein products and essences and flavorings. This demand in turn appears to be driven by fast but uneven growth of China's food processing industries. In many cases, food manufacturers' capabilities have outstripped those of the supporting industries that supply their ingredients. Anecdotal evidence indicates that these supporting industries are developing quickly, and the window for exporting some of these specialized ingredients may be narrowing. Others, however, like certain essences and flavorings, are likely to remain a long-term growth market.

Tables

Table 1. U.S. Exports of Consumer-Oriented Ag Products to China, 1998 – 2003								
	Year						% of total	
	1998	1999	2000	2001	2002	2003	1998	2003
Other Cons. Oriented	19,313	18,334	34,583	58,354	41,975	135,645	15.9%	30.9%
Poultry	28,889	42,093	35,994	29,575	42,621	72,272	23.7%	16.4%
Processed Frt & Veg	9,337	15,883	25,734	34,134	43,328	59,498	7.7%	13.5%
Red Meat F/C/F	15,278	15,192	22,099	40,532	45,805	46,867	12.6%	10.7%
Dairy	13,908	17,748	22,302	40,267	32,135	38,869	11.4%	8.8%
Fresh Fruit	11,333	1,866	23,147	29,059	24,280	33,335	9.3%	7.6%
Snack Foods	8,549	14,020	20,425	18,208	15,305	17,811	7.0%	4.1%
Tree Nuts	2,337	3,702	8,895	10,164	18,554	15,080	1.9%	3.4%
Pet Food	490	977	1454	3,390	5,822	6,540	0.4%	1.5%
Fruit & Veg. Juices	1,490	1,734	1,223	2,451	5,347	4,248	1.2%	1.0%
Wine & Beer	2,404	3,826	1,420	2,697	3,260	2,828	2.0%	0.6%
Breakfast Cereal	508	323	661	861	1,459	2,085	0.4%	0.5%
Fresh Vegetables	3,735	3,657	5,080	3,005	788	1,662	3.1%	0.4%
Red Meat P/P	2918	1,125	863	783	200	1,240	2.4%	0.3%
Eggs	139	340	266	1,118	523	870	0.1%	0.2%
Nursery Products	1,029	1,358	1,129	1,025	1,462	598	0.8%	0.1%
Source: U.S. Customs Data								

Table 2. Key components of 'Other intermediate products' including Chinese tariffs and taxes and tariff code equivalents						
Product	Tariff line(s)	2002 Exports	2003 Exports	Growth (%)	Tariff/ VAT (%)	Comments
Conc. And textured protein substances	2106100000	11,679	31,675	171	10/17	
Odoriferous substances and mixtures, for use in food	3302100000	14,488	31,294	116	15/17	Matches China Customs line 3302101000.
Chicken feet and other offal	0207140045	6,051	29,599	389	RMB 0.5 per kilo/13%	No exact match. Used 'frozen chicken offal other than wingtips' (0207.1411.00)
Protein isolates	3504001000	8,026	22,923	186	3/17	Peptones and other proteins, NES
Animal/veg. fats & oils nesoi	1518000000	6,901	21,587	113	10/17	
Guts, bladders & stomachs, not ovine	0504000020 0504000040	15,475	20,475	32	18-20/13	No exact match, but tariffs under 0504 generally run 18-20%
Edible gel & photo gel, nesoi	3503005040	8,609	16,120	87	12/17	No exact equivalent
Flour and meal from poultry meat	2301100000	28,810	14,311	-50	2/13	No exact match. Used 2301.1019.00
Essential oils (peppermint, etc.)	3301xxxxxx	16,810	13,302	-21	20*/17	* Citronella, sassafras and 'other mint' have lower tariffs.
Vegetable saps & extracts (incl. hops)	1302120000 1302130000 1302190000	4,364	10,880	149	Mostly 20/17	No exact match. The closest Chinese category includes ephedra and lacquer.